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In the

Supreme Court of the United States

OCTOBER TERM, 1972

No. 72-1150

IN THE MATTER OF DALLAS CABANA, INC., Bankrupt
JEROME B. ROSENTHAL, ROSENTHAL and GREEN
CABANA MANAGEMENT, INC. and DALLAS CABANA,
INC. (Bk-3-1210),

Petitioners,

v.

WILSON F. COLLIER, Trustee,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPPEALS FOR THE FIFTH CIRCUIT

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TABLE OF CONTENTS

	Page
Opinion Below	1
Jurisdiction	2
Questions Presented	2
Statement of The Case	3
Reasons for Granting a Writ	8
I. The Rulings below conflict with principles of decisions by this Court and involve important principles of Federal Law that should be resolved by this Court.	8
A. Conflict of Interest	9
B. Power of Referee to summarily terminate hearing on claims and punish creditor claimants for conduct of interested witness.	15
Conclusion	20

Page

Bankruptcy Jurisdiction: Is it Too Summary, So. Calif. L. Rev. 78 (1966) 14

Carlyle Packing Co., 12 F. Supp. 8 (W. D. Wash. 1935) 12

In re Forester, 222 F. 537, 538 (N. D. Calif. 1950) 12

In re Green, 369 U. S. 689 15

Holt v. Virginia, 381 U. S. 131 15

Hovey v. Elliott, 167 U. S. 409 15

Illinois v. Allen, 397 U. S. 337 15

Mayberry v. Pennsylvania, 400 U. S. 455 15

Mosser v. Darrow, 341 U. S. 267 12

In re Oliver, 333 U. S. 257 15

Proceedings of Seminar for Referee in Bankruptcy 14

Ungar v. Sarafite, 376 U. S. 575 15

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Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPPEALS FOR THE FIFTH CIRCUIT

To the Honorable Supreme Court of the United States:

The Petitioners respectfully pray that a Writ of Certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Fifth Circuit entered on November 10, 1972.

OPINION BELOW

The opinion of the United States Court of Appeals, ... F. 2d , not yet reported, appears in the Appendix to this Pe-

tition. The judgment and order of the District Court, not reported, appears in the Appendix to this Petition. The Certificates of Review and the Order of the District Court appear in the Appendix (Vol. 1 and 2) of the record below certified to this court at (App. 155-241) (App. 250-256) (App. 298-314) (App. 324-415).

JURISDICTION

The judgment of the United States Court of Appeals for the Fifth Circuit was entered on November 10, 1972. A timely Petition for Rehearing and Rehearing en Banc was denied on December 29, 1972. This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

QUESTIONS PRESENTED

1. Whether the Petitioners were entitled to a hearing on any of their several motions to disqualify counsel for the Trustee and removal of the Trustee for such disqualification, where counsel for the Trustee, who were also counsel for the bankrupt, allegedly had failed to comply with General Order 44 (requiring disclosure of all facts that could give rise to a conflict of interest between creditor, debtor, trustee, and any interested parties and their attorneys).

2. Whether the Referee in Bankruptcy may, without a hearing or show cause order, summarily punish two creditor claimants by the termination of the hearing on claims (without the completion of the testimony of a single witness), the denial of some two million dollars in claims, and the imposition of a cross-judgment, because the Referee personally deemed the action

and conduct of an interested witness to be improper and offensive (which action included the unsuccessful efforts to secure a hearing on the asserted conflict of interest).

STATEMENT OF THE CASE

The two questions presented at bar arise out of Bankruptcy proceedings relating to Dallas Cabana Motor Hotel and especially the disputes concerning ownership, obligations to and from, and control of the hotel between two rival factions, the Melcher group (Doris Day Melcher, the Estate of Martin Melcher and various entities that they control) and the petitioner-Rosenthal interests (Jerome B. Rosenthal, Rosenthal and Green, and Cabana Management, Inc.). Rosenthal had acted as an attorney and advisor to the Melchers in reference to the Atlanta, Dallas and Palo Alto Cabana Hotels. Following the death of Martin Melcher, the business and professional relationship rapidly deteriorated into bitter disputes, fanned by hotly contested and multiple litigation proceedings. (R. 599, 622) Previously the Melchers had advanced substantial funds for financing and operating the Cabana Hotels, but had received a slightly larger benefit of over two million in cash tax savings. The tax savings were predicated on the basis of partnership ownership of the hotel, with record or legal title in the name of Dallas Cabana, Inc., a partner. (R. 2352, 2356)

The Melcher interests demanded that Rosenthal file a Chapter XI proceeding for the hotel. (R. 1518) When Rosenthal hired independent counsel to file the Chapter XI rather than the attorney selected by the Melchers, the Melchers, on stockholder notice only to themselves, purported to take control of Dallas Cabana, Inc. and caused a second Chapter XI to be filed by

their attorneys. (R. 590) The Referee consolidated the two proceedings but to this day has never determined which of the two Chapter XI Petitions was the proper one or which group had the authority to act for Dallas Cabana, Inc. The Melcher and Rosenthal interests were in discord and the Referee ended the Chapter XI proceedings by summarily adjudicating Dallas Cabana, Inc. a bankrupt. (R. 607)

The same Melcher attorneys who had filed the second Chapter XI, in addition to representing the bankrupt, were appointed special and later co-counsel to the Trustee and concurrently XIacted in such capacities. (R. 289) In purported compliance with general Order 44 which requires affirmative disclosure under oath of "all of the attorney's connected with the bankrupt or debtor, the creditors or any other party in interest and their respective attorneys", the only factual report was the retainer fee advanced by Doris Day Melcher on behalf of Dallas Cabana, Inc. In the orders of appointment, all other possible conflicts of interest were catagorically denied.

The Melcher counsel were first appointed special counsel for the Trustee in reference to the title question; viz, whether the equitable ownership of the hotel was in a partnership (as claimed by the Rosenthal interest), or in the record title holder, Dallas Cabana, Inc., (as claimed by the Melcher interests). The Referee ruled that the equitable ownership of the hotel was in the corporation. (R. 625) Subsequent orders of the referee affirmed the sale of the hotel to Pritzker (Hyatt Hotel interests). (R. 625) The conflict of interests issue of having counsel for the bankrupt also represent the Trustee was first raised in the Petition for Review of the Order on Title. (R. 587)

Subsequent to the appointment of the Melcher counsel as co-counsel for the trustee and the sale of the hotel to Pritzker, it was discovered that certain connections involving interested parties had not been disclosed as required under General Order 44. The Melcher attorneys had an undisclosed meeting with Pritzker, a prospective purchaser of the Dallas and Palo Alto Hotels. At this meeting it was agreed that Pritzker would purchase the Dallas Hotel for a little over four million dollars and obtain good title through Bankruptcy proceedings to be filed. Under this procedure, Rosenthal's claim of partnership ownership would be determined by the Referee instead of a state court. (R. lappen, Dep. 10-27-69, p. 91-95, 102, 107-118)

Prior to the hearing on credit of claims and as soon as practical after the discovery of the non-disclosure of the conflicts of interests, a motion to disqualify certain counsel for the Trustee was filed with the Referee. (R. 1948) A Motion to shorten the time for hearing was also filed and a subsequent Motion was filed for hearing on December 8, 1969. A letter concerning the conflict of interest was addressed to the Referee (with copies to opposing counsel and the District Judge before whom the first Certificate of Review was pending). (R. 2021)

On December 8, 1969 the Referee, in reference to the disqualification motion, denied petitioners the right to call witnesses and conduct an evidentory hearing. (R. 2025-3071) The Referee summarily denied the motion and reprimanded counsel for having sent a copy of the letter to the district judge. (R. 2021) A Petition for Review was filed and in addition the same Motion for Disqualification was filed in the District Court with a supporting brief containing detailed statements of facts

as well as legal authorities. A written request for a hearing before the district judge was made. (R. 3240-56) A subsequent Motion was also filed with the Referee requesting that the Trustee and his appointed counsel comply with General Order 44. (R. 3247) This motion was also summarily denied and timely Petition for Review was filed. In further attempts to secure a hearing on the conflict of interest, petitioners made written requests for a pre-trial conference with the District Judge, filed another Motion for disqualification in the District Court, filed a Motion to remove the Trustee because of the disqualification of certain counsel, proferred in evidence the depositions that related to the disqualification, sought leave for further discovery relating to the conflict of interest issue, and in writing, requested a hearing on disqualification either by itself or in conjunction with the orders of the Referee on adjudication, title, etc. (R. 3240) The Trustee filed no motion either before the Referee or the District Judge in connection with the sufficiency of the pleadings on disqualification and filed no answer either admitting or denying the allegations of the motions.

While matters relating to disqualification of the Melcher counsel were pending before the District Court, the creditors claims of Cabana Management and Rosenthal and Green (Jerome B. Rosenthal is not a creditor but is interested in the claims) were being contested by the Trustee through the Melcher counsel. Before completion of these hearings and indeed without the completion of the examination of any of the three witnesses who had been called to testify, the Referee, because of conduct and actions of Rosenthal, terminated the hearing. He also denied all the creditor claims of Cabana

Management and Rosenthal and Green, and entered a cross judgment against the Rosenthal interests. (R. 3152-3239) The Referee in summarily terminating the hearing did not certify Rosenthal's conduct as being contemptous within 11 U.S.C. §1169 (which would have afforded Rosenthal the right of a hearing before a District Judge) nor was any show cause order issued by the Referee. No right was accorded Petitioner to respond to any specific charges. The Referee's subsequent Certificate of Review attempted to justify such action in some twenty (20) pages of a subjective factual and legal analysis. This involved (1) the previous actions and conduct of Rosenthal including the filing of his Motion for Disqualification; (2) the action and conduct of Rosenthal at the creditor claims hearing, which including an attempt to obtain a continuance because at the time Rosenthal was seeking to press the disqualification of counsel for the Trustee, an investigation against Rosenthal was being conducted by the F.B.I. which could be authorized by the Trustee through counsel under 18 U.S.C. §3057; and (3) the friction that developed between Rosenthal as a witness and counsel for the Melcher interests who were counsel for the Trustee at the claims hearing and (4) because of friction between Rosenthal and the Referee. (R-3152-3239)

The items that were reflected in the creditor claims of Cabana Management and Rosenthal and Green had been previously utilized and treated by Doris Day Melcher and her late husband as valid and legally owed in federal income tax returns. Because the partnership was on an accrual basis and the Melchers on a cash basis the unpaid claims had resulted in a cash tax savings (R. 2352-2356) The tax returns had been audited and approved by the IRS after consultation with the Melchers. (R. 2352) In

the Bankruptcy Court, the Melchers through their counsel, representing the Trustee, urged that the claims of Cabana Management and Rosenthal and Green be denied so that the Melcher interests, who had disputed creditor claims themselves, could receive money from the estate. The efforts were successful.

The first Certificate of Review had been filed in the District Court on May 12, 1969. (R. 587-638) The fourth and last Certificate of Review, to date, was filed on May 7, 1970. (R. 3152-3239) While the various requests of the Petitioners for a hearing before the District Judge were pending, Petitioners subpeonaed counsel for the Trustee for a deposition. A protective order was sought before the Referee (R. 3372-3381) and Petitioners then sought in the District Court a writ of prohibition. (R. 3371) The District Judge stayed discovery, directed the parties to file on outline of all issues, and set oral argument by counsel on all four Certificates of Review for November 3, 1971. (R. 3403) On such date and at the conclusion of argument, the District Judge affirmed in toto the orders of the Referee and summarily denied all of the disqualification motions filed in the District Court. (R. 3482) A timely appeal was taken and the action of District Court was affirmed by the Fifth Circuit. (R. 3486) The Petition for Rehearing and Rehearing en Banc was denied. A motion to stay the mandate pending certiorari was granted.

REASONS FOR GRANTING A WRIT

I. RULINGS BELOW CONFLICT WITH PRINCIPLES OF DECISIONS BY THIS COURT AND INVOLVE IMPORTANT PRINCIPLES OF FEDERAL LAW THAT SHOULD BE RESOLVED BY THIS COURT.

A. CONFLICT OF INTEREST

There is no dispute that the Referee and the District Court below summarily denied the Petitioners' effort to disqualify counsel for the Trustee on allegations of their relationship with the bankrupt and Melcher interests who were disputed owners, shareholders, partners, obligators and creditors of the bankrupt. No reasons or findings of fact or conclusions of law were made by the District Court in its order denying the Motions filed therein and its affirmance of the Referee's Orders on the Certificate of Review was without further comment. Rosenthal contended that the Melcher interests wanted to sell the Hotel to Pritzker, and discovered that at an undisclosed meeting a deal had been made to sell the assets of the Estate and that the bankruptcy forum would be used to give good title. (A major problem if partner ownership was recognized because there were solvent partners and the property, absent consent, could not be administered in the bankruptcy forum). Motions to Disqualify were pressed before the Referee; however, the Referee allowed no evidentuary hearing on the Motion, and with the exception of general comments, made no finding of fact or conclusions of law evidencing consideration of the merits of the matter.*

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* "4. The denial of the Motion to Disqualify counsel is a valid and proper exercise of the discretion of the Referee in bankruptcy." Vol. 2 Appendix p. 309. "The Motion to disqualify them alleging a conflict of interest was filed on November 28, 1969 only a few days before the date set for the hearing on those matters, and after much discovery and preparation for a hearing had been made. The effect, if not the purpose of the motion, if granted, would have been to cause additional delay and expense.

After hearing the argument of counsel, Mr. VanDercreek, in support of the Motion, and Mr. Trost in opposition, I was opinioned that there was no substantial good objection to representation of Trustee by Messrs. Rochell and Trost and that in the exercise of a proper discretion the Motion should be overruled." Vol. 2 of the Record Appendix, P. 313-314.

Implicit in the holdings of this Court in such cases as *Commonwealth Coatings Corporation v. Continental Casualty Co.*, 393 U.S. 145 and *In re Murchison*, 349 U.S. 133, would be the right to a fair hearing upon charges of conflict of interest. *Murchison* involved a question of judicial disqualification in which this Court stated "A fair trial in a fair tribunal is a basic requirement of due process. Fairness, of course, requires an absence of actual bias to the cases tried. But our system of law has always endeavered to prevent even the probability of unfairness. To this end no man can be a judge of his own case and no man is permitted to try cases where he has an interest in the outcome. That interest common be defined with precision. *Circumstances and relationships must be considered* * * *" (Emphasis added.) 349 U.S. at 136.

If in determining a conflict of interest, circumstances and relationships must be considered it would necessarily follow that a fair hearing with the taking of evidence would be necessary. The rulings of the tribunals below are in conflict with the above principles unless they are inapplicable, as a matter of law, to federal bankruptcy proceedings. Petitioners submit that not only are the general principles of conflict of interest and due process fully applicable to the Trustee, an officer of the Court, and his counsel, but that by statute and general orders of bankruptcy there is an express duty of the Referee to avoid such conflicts as result where the attorney for the bankrupt is also attorney for the Trustee. This Court once stated "Many abuses have occurred in the bankruptcy practice, and none is more frequent than that by which the attorney for petitioning creditors becomes counsel for the trustee subsequently appointed.

This mingling of interests, frequently conflicting, is generally regarded by courts as working to the detriment of one of the parties and to the undue advantage of another. Experience has shown the wisdom and necessity of separating the function and obligation of counsel by forbidding the employment in different interests of the same person. In this way only may the court be advised how conflicting interests are represented." *Weil v. Neary*, 278 U.S. 160, 168.

Although counsel for general creditors is now by statute not automatically disqualified to act as counsel for the Trustee, (11 U.S.C. § 72(c)), no such provision exists in reference to counsel for the bankrupt corporation. To the contrary, 11 U.S.C. § 72(a) prohibits a bankrupt corporation's directors, officers or shareholders from even voting to select a Trustee. Counsel retained by the Melcher interests to represent the bankrupt corporation (Dallas Cabana, Inc. Bk. 3-1213 consolidated with Bk. 3-1210) and who still purports to do so also became counsel for the Trustee. "Former attorney for bankrupt should not be appointed". Referee Kineson, *Notes on Conduct of Election for Trustee*, 40 *J. Nat. Assn. Conf. Bkr.* 115, 119 (1966)

The purpose of General Order 44 is for the Trustee and his counsel to make full disclosure of the facts so that the Court can consider if the conflict exists. The Trustee and counsel are not unilaterally to decide there is no conflict and conceal the facts by which they reach such decision.

Although the right to a hearing because of non-disclosure of potential conflicts of interests would be implicit under general principles of due process, petitioners submit that it is expressly

provided for in bankruptcy situations. Upon notice and hearing at any time during bankruptcy proceeding, federal courts are expressly charged, upon complaint of petitioning creditors, with the jurisdiction and duty to remove a Trustee for cause. 11 U.S.C. § 11(a)17) Under the power conferred by the above section the Second Circuit removed a Trustee and vacated all orders because of a conflict of interest. Se in re Freeport Italian Bakery, Inc., 340 F. 2d 50, 55 (1965):

> "* * * If the administration of the estate in bankruptcy would suffer more from the discord created by the present trustee than would be suffered from a change of administration, the removal of the trustee is necessarily the better solution.
>
> "We reverse the order denying the removal of Dominick Cataldo as trustee, direct his removal forthwith, and direct the appointment as trustee of some person having no previous connection with any of the parties in this bankruptcy proceeding. * * *"

Other lower courts have recognized that removal of trustee is proper where its counsel is disqualified. See e.g. in re *Carlyle Packing Co.*, 12 F. Supp. 8 (W. D. Wash. 1935) and *In re Forester*, 222 F. 537, 538 (N. D. Calif. 1950). Petitioners would submit that this Court should rule that non-disclosure in violation of General Order 44 is grounds for a hearing and removal of trustee under 11 U.S.C. § 11(a)(17).

In *Mosser v. Darrow*, 341 U.S. 267 this Court in reversing the Seventh Circuit held that a former Trustee who "did not disclose" (341 U.S. at 274) possible conflicts of interest of certain of his employees, rendered the former Trustee personally liable for substantial surcharge, even though the Trustee him-

self received none of the profits nor was guilty of any wrong doing.

In the case at bar not only did the Melcher attorneys represent the bankrupt and the trustee, but the Melcher interest had filed substantial creditor claims which were disputed. In reference to this plurality of interest counsel for the Rosenthal interest wrote to the referee in bankruptcy on December 2, 1969: "If the Melcher attorneys are going to be paid out of the estate for opposing Rosenthal claims, then likewise it could seem that the Rosenthal attorneys should receive their compensation as a priority administration fee for opposing the Melchers." (R. 2019)

In reference thereto the Referee stated:

"But, the suggestions that the attorney should be paid a fee for opposing the Trustee seems to be rather preposterous and Mr. Rosenthal will receive from the estate whatever he proves he is entitled to but he is not going to get anything more or less." (R. 2020)

Since the proceeds that do not go to Rosenthal are claimed by the Melcher interests, it would seem equally obvious and preposterous for the Melcher interests to represent the Trustee.

In a seminar for Referees in bankruptcy, sponsored by the administrative office of the United States Courts, it has been stated; "The most fundamental requirement for the Trustee is impartiality * * * and there can be very little doubt in our mind as to the sufficiency of cause for disapproval for the Trustee closely associated with the creditor who has a voidable preference, a lien of dubious validity or a disputed claim * * *" *Pro-*

ceedings of Seminar for Referees in Bankruptcy, Administrative Office, U. S. Courts (1965) Vol. 2, p. 228, 229

Substantial recognition that he who represents a Trustee is apt to win before the Referee is found in an article by a partner of the counsel at bar representing the bankrupt and the Trustee.

George M. Treister, *Bankruptcy Jurisdiction: Is it Too Summary,* 39 *So. Calif. L. Rev.* 78 (1966), reprinted 40 *J. Nat. Conf. Ref. In Bkr.* 80 (1966).

> "Nevertheless, there still remains a defect in the bankruptcy structure. My criticism is directed at that aspect of the system which, in operation, asks one judicial officer — the Referee — not only to decide litigated questions, but also to preside over discovery proceedings and to perform extensive administrative functions and other duties not normally imposed upon Judges. The potentialities inherent in this, despite the absence of any personal financial incentives, *makes the bankrutpcy court in many cases an unattractive place in which to do battle with a Trustee.* 39 So. Calif. L. Rev. at 85-86. (emphasis added)
>
> "Conceding that a Referee would not intentionally speak about controversial matters with one adversary party in the absence of the other, nevertheless it is undesirable for a judicial officer to have the frequent informal contacts which his administrative duties necessitate. There is too much of a chance, despite all good intentions and efforts, that what is learned or suspected outside of court may have some influence on the judicial decision. *It may be only a subtle or even subconscious influence, but a bell cannot be unrung.* Adverse claimants have at least some reason to fear that their trial in the Referee's Court might not start on a completely clean slate. *Id.* at 87. (Emphasis added)
> "The constitutional guarantee of due process of law applies in the bankruptcy court, of course, as well as anywhere

else. At a minimum, due process demands adequate notice of the issues and the right to a fair hearing. *Id.* at 83.

B. POWER OF REFEREE TO SUMMARILY TERMINATE HEARING ON CLAIMS AND PUNISH DEBTOR CLAIMANTS FOR CONDUCT OF INTERESTED WITNESS.

The Referee below chose to summarily end the claims proceedings and to deny creditor claims of the Rosenthal interests for over two million dollars, that had been corroborated by the Melcher income tax returns, and to enter a cross-judgment. This Court traditionally has been cautious about the power of Judges to summarily inflict punishment for contempt. See, *e.g.*, *Ungar v. Sarafite*, 376 U. S. 575; *In re Green*, 369 U. S. 689; *Illinois v. Allen*, 397 U. S. 337; *Holt v. Virginia*, 381 U. S. 131; *Mayberry v. Pennsylvania*, 400 U. S. 455; and *In re Oliver*, 333 U. S. 257.

The power of the Referee to exercise contempt power, at best, is considerably more limited than that of a federal district judge. Congress by statute has expressly provided that in the case of contempts before Referees that the facts are to be transmitted "forthwith" to the district judge for a hearing "to show cause why he should not be adjudged in contempt by reason of the facts so certified." 11 U.S.C. § 69. The Referee in the case at hand did not certify any facts for a contempt hearing as authorized by the statute.

Petitioners would submit to this Court that under the above section, the Referee, himself, does not have contempt power. In addition, this Court has held that a contempt is not to be punished by the denial of a hearing on a party's claim. *Hovey v.*

Elliott, 167 U. S. 409. What the Referee can not do directly by contempt, he should not be able to do under the guize of some other label. Moreover, notwithstanding the significant question of whether the Referee has the power under some basis to go act, the basic question would remain whether the Referee may summarily act as was done at bar without a show cause order affording the Petitioners the right of a hearing to respond to specific charges. The power of the Referee to control hearings should be balanced against the rights of parties to basic concepts of due process.

In *Holt v. Virginia*, 381 U. S. 131, a contempt proceeding evolved out of unsuccessful efforts to seek a change of venue and to disqualify a state judge for bias. In the case at bar, the Referee noted the efforts to disqualify counsel and to seek a change of venue as reasons for terminating the hearing and denial of the creditor claims.* This Court in *Holt* held the party had a constitutional right to a hearing with counsel and with opportunity to present evidence.

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* "35. On the first day of trial, December 8, 1969, Rosenthal's counsel argued the motions to transfer the proceedings to California, and to disqualify counsel for the Trustee. The motion to transfer was overruled, as was the motion to disqualify. It was also on December 8 that the court commented upon the disrespect shown to it by Rosenthal and his counsel, in connection with his counsel's letter of December 2, 1969, to the District Judge, in which he made the outrageous statement that this court was controlled by the Melchers." R. 3170

"41. The court's hopes that Rosenthal's attitude toward the proceedings would improve during the recess in the trial from December 17, 1969, to March 2, 1970, were soon disappointed. Rosenthal did not appear in court on March 2, but rather, additional motions were presented by his counsel in an attempt to prevent this court from concluding the evidence on the objections to claims This time Rosenthal sought a continuance until the certificate on review from all other matters was decided and because of the investigation of Rosenthal by the Federal Bureau of Investigation. Disqualification of the trustee's counsel was again re-

In similar vein, this Court in *In re Green*, 369 U. S. 689, held that a conviction for contempt without a hearing and an opportunity to refute charges violated federal due process. Although this Court has ruled that a state court judge who characterized a witness's conduct as contemptuous, disorderly and malingering was not as a matter of law constitutionally disqualified to hear the contempt charges, the opinion was careful to note that the contempt proceedings were non-summary with due notice and full opportunity for a hearing to refute charges. *Ungar v. Sarafite*, 376 U. S. 375. Under this Court's decisions where the judge becomes personally embroiled, not only must a non summary hearing be held, but personal attacks may require such hearing to be held before a different judge. See *e.g., Mayberry v. Pennsylvania*, 400 U. S. 455 and *In re Oliver*, 333 U. S. 257.

The Referee below filed four Certificates of Review (in response to over eleven Petitions for Reviw on orders on title, sale etc). Approximately one half of the total (123) pages of the

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quested. Other dilatory motions were also filed: For the first time, Rosenthal moved to require the trustee to produce certain accounting work papers and the books and records of the Palo Alto Cabana, moved to require the trustee's counsel to file additional affidavits on the issue of disqualification and, in any event, moved for a continuance of the proceedings until Wednesday *on the grounds that Rosenthal and Harrison were in California and not in Dallas.* All of these motions were overruled, and the court instructed Rosenthal to take the stand on Tuesday, March 3, at 9:30 A.M." R. 3173

"43. After that short recess, Rosenthal's counsel advised the court that Rosenthal would take the stand under protest and only on condition that his counsel could make a statement for the record. Rosenthal's counsel then reiterated the motions for continuance based upon (1) the alleged conflict of interest of the attorneys for the Trustee; and (2) the Federal Bureau of Investigation's investigation of Rosenthal. Both motions were again overruled." R. 3174

Certificates were devoted to a highly prejudicial diatribe against Rosenthal. Many of the attacks by the Referee were on collateral matters that were not directly related to the substantive issues before the Court. Upon the filing of the first Certificate of Review, which contained such matters, Petitioners promptly filed written objections with the district court requested a *hearing* for opportunity to refute the charges — to no avail.

The charges of the first Certificate were utilized by the Referee in the fourth Certificate to bolster his reasons for terminating the creditor claims hearing of Cabana Management and Rosenthal and Green. The Referee also relied upon the friction that arose between Rosenthal as a witness and the Melcher attorney who were representing the Trustee. Such friction could hardly be avoided because if the Melcher counsel were successful in baiting Rosenthal and causing the Referee to terminate the hearing and deny the claims being presented, the Melcher interests for their own disputed claims would then receive substantial sums from the Estate. A fact in itself that should suggest the need for a hearing on the Referee's actions.

Under the precedents of this Court previously discussed, the very comments of the Referee requires a hearing. The accuracy of the charges should be determined with opportunity for the Petitioners to present evidence in their behalf. Some excerpts from the Referee's Certificates are quoted in a footnote.*

Although bankruptcy is the exclusive responsibility of the federal courts, bankruptcy, as this court knows, is the step-child

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* "47. Not only was Rosenthal's conduct during the claims litigation characterized by the same disrespect for the court and for opposing

of the federal judiciary — often unwanted and largely ignored. Although the over 200,000 filings of bankruptcy proceedings suggest the importance of the area, the problem of effective appellate review virtually preclude the traditional role of the appellate courts. Indeed, as in the case at bar, the Referee in bankruptcy, who is *not* an Article III Judge, is fast becoming the court of last resort. The importance and responsibility for this Court to insure that conflicts of interests are avoided and that the parties are afforded a fair hearing in bankruptcy would seem far greater under principles of federalism than that which exists by this Court in reference to state court proceedings. If a party can be denied a hearing on a charge of conflict of interest and then be denied all claims for alleged misconduct, again without the benefit of a hearing on such charge, as was done at bar, the need for action of this Court is at hand. To punish a person for asserting a conflict of interest, will certainly restrict in allegations in the future but it will also multiply undisclosed conflicts.

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counsel which had characterized it during previous matters in this proceeding, but Rosenthal's propensity to make material misrepresentations to the court continued as well. A dramatically clear illustration in this regard occurred during Rosenthal's testimony under oath regarding the amount of the Rosenthal and Green claim. Rosenthal testified on at least three different occasions that his firm had never been paid any amount whatsover for legal fees due from the Dallas Cabana. In truth and in fact, Rosenthal's own files contained a letter from his secretary acknowledging the receipt of *$20,000* from the Dallas Cabana hotel *"for legal services to date."* R. 3179

Note: Contrary to the statement of the Referee, the creditor claims of Rosenthal and Green that were filed in the court expressly credited the $20,000 in reference to Palo Alto. R. 3233

CONCLUSION

For the foregoing reasons the Petition for Writ of Certiorari to the United States Court of Appeals should be granted.

Respectfully submitted,

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APPENDIX

In the

United States Court of Appeals

FOR THE FIFTH CIRCUIT

No. 72-1273

In The Matter of: DALLAS CABANA, INC., Bankrupt.
DALLAS CABANA, INC., ET AL,

Appellants,

versus

WILSON F. COLLIER, Trustee,

Appellee.

Appeal from the United States District Court for the Northern District of Texas

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(November 10, 1972)

Before GEWIN, THORNBERRY and CLARK, Circuit Judges.

CLARK, Circuit Judge: This is an appeal from the final order of the district court affirming the Findings and Conclusions of the Referee in Bankruptcy in regard to proceedings involving Dallas Cabana, Inc. The proceedings were factually complex and hotly, indeed vituperatively, disputed. A lengthy and detailed opinion could serve no precedential purpose to the public and the underlying facts are too well known to the litigants to be of benefit to them. We have therefore distilled our opinion to its legal essence.

The premier issue in this case — to which the other points assume secondary importance — is whether the equitable

title to certain hotel property in Dallas, Texas, was vested in the bankrupt at the time of adjudication. The trustee made the issue through his institution of a quiet title proceeding in which he readily met his burden of proof by showing legal title to be in Dallas Cabana, Inc., the bankrupt. However, proof of legal title was not sufficient to finally dispose of the question in the case at bar because under Texas law the trustee possessing the powers of a judgment creditor (but not a bona fide purchaser for value) under Section 70c of the Bankruptcy Act[1] cannot prevail over an unrecorded equitable interest in real estate.[2] While Appellant Rosenthal necessarily conceded that the bankrupt held the legal title, he affirmatively contended that such title was held in trust for a partnership or joint venture and that equitable title was vested in the individual partners or joint venturers; thus, the property was improperly included in the bankrupt's estate.

To prevail on his contention, Rosenthal was required to show that, first, the partnership or joint venture existed at the time the bankrupt corporation took legal title and, second, the bankrupt acquired its legal title with an equitable charge to hold the same for the benefit of the partnership or joint venture. The referee made no finding as to the first point. However, as to the second sine qua non, the referee's findings demonstrate that Rosenthal did not carry his burden of showing that the alleged partnership or joint venture held any equitable interest in the hotel property.

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[1] 11 U.S.C.A. § 110(c) (Supp. 1972).

[2] See, e.g., Hammett v. McIntire, 365 S.W. 2d 844 (Tex. Civ. App. 1962), error refused; Roeser & Pendleton v. Stanolind Oil & Gas Co., 138 S.W. 2d 250 (Tex. Civ. App. 1940), error refused; South Texas Lumber Co. v. Nicoletti, 54 S.W. 2d 893 (Tex. Civ. App. 1932), error dismissed; Del Rio Bank & Trust Co. v. Cornell, 57 F. 2d 142 (5th Cir. 1932).

The referee found that "the investors were not certain what type of equity interest they had in the hotel" and that no limited partnership agreement was ever prepared. The stock of Dallas Cabana, Inc., which held legal title to the property, was held by three people who "do not know and have never known for whom they are holding the shares of stock that stand in their names." The entities which made substantial extensions of credit to Dallas Cabana, Inc. were unaware of any sort of partnership or joint venture arrangement. Even were we to assume the existence of the partnership, it does not follow that that entity held equitable title to the property itself, rather than merely holding some nebulous equity in the title to the stock in Dallas Cabana, Inc. Rosenthal failed to establish that any partnership or joint venture held any equitable interest in the hotel property.[3]

Rosenthal contends that counsel for the Melcher interests were improperly retained by the trustee for the purpose of litigating the issue as to the trustee's title to the hotel property. This, it is urged, created such a conflict of interest in the administration of the estate that the trustee should have been removed and his orders vacated. The conflict of interest is alleged only in general terms, and Rosenthal's briefs do not reveal any actual conflict of interest between

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[3]Rosenthal bases much of his case on the existence of partnership tax returns which reflected claimed deductions for partnership losses by his true rival in these proceedings who is not the trustee, but the so-called Melcher interests. These tax returns were prepared by Rosenthal while he was attorney and financial manager for the Melcher Interests, attorney and financial manager for Dallas Cabana, Inc., and a director of Dallas Cabana, Inc. In a post-argument brief Rosenthal points out that the Melcher interests have claimed a partnership existed as to prior similar hotel ventures. While the returns and prior similar business undertakings provide some support for Rosenthal's contention, neither separately nor together would they have compelled the referee to reach an opposite resolution of the disputed title issue.

the trustee and the Melcher interests as to the title question. Indeed, it appears that the interests of both perfectly coincide as to this facet of the proceedings — the Melcher interests as well as the trustee desired to retain the hotel property as part of the bankrupt estate. General counsel to the trustee, whose status and qualifications are attacked, also advised him that the title contentions of the Melcher interests were apparently correct in fact and law and that the employment of the Melcher attorneys would be in the best interests of the general creditors. The objective of employing the Melcher counsel was to save time and expense by acquiring the benefit of the already existing familiarity of these counsel with the factual situation pertinent to the title issue. The referee did not err in approving the trustee's action in employing counsel for the Melcher interests for this purpose.

Rosenthal next urges that the referee erred in adjudicating Dallas Cabana, Inc. (which had voluntarily entered the bankruptcy forum seeking a corporate reorganization under Chapter XI) a bankrupt without giving the notice and hearing required by Section 376 of the Bankruptcy Act.[4] The evidence shows that the notice of the First Meeting of Creditors in the Chapter XI Reorganization proceedings contained a notice that the court could at that first meeting, or at any continuation thereof, adjudicate bankruptcy or dismiss should the Arrangement fail.[5] The referee entered

[4] 11 U.S.C.A. § 776 (1970).

[5] Two Chapter XI petitions were filed by attorneys purporting to represent Dallas Cabana, Inc. the first to be filed was the one prepared by attorneys representing Rosenthal, and the second was by counsel representing the Melcher interests. The two petitions were consolidated for procedural purposes, but the issue of which petition would finally govern was never resolved. The Melcher interests consented to the bankruptcy adjudication, but Rosenthal did not. However, Rosenthal never moved to dismiss or withdraw the Chapter XI petition which he procured.

an order of adjudication at a continuation of that meeting after determining that an Arrangement which would salvage the corporation was impossible and that bankruptcy was in the best interests of the creditors. Appellant has failed to show significant prejudice resulting from the allegedly defective notice which warrants reversal by this court. There is no serious contention that Dallas Cabana, Inc. should not have been adjudicated a bankrupt. If there was some actual prejudice to Rosenthal from the allegedly defective notice, the appropriate remedy at this time is most certainly not to invalidate the adjudication post hoc. The factual issues which Rosenthal asserts he would have interposed in the hearing on the adjudication have now been resolved against him in proceedings of which he was duly notified and in which he fully participated. It would be pointless to now reverse the referee's adjudication on this technicality.

Since the issues discussed above are resolved in favor of the Trustee, we reject the appellants' contention that the referee's confirmation of the sale of the property should be set aside.

For these same reasons given with regard to the title claim representation, time and expense, the special counsel was also employed to contest the creditor claims of the Rosenthal interests. The trustee, after receiving the advice of his independent general counsel that the claims for legal and financial services were unsupported, determined that litigation of this detailed and complicated matter could best be conducted by those already familiar with the nature of the business operations of the bankrupt. While acknowledging the rule to be that counsel for the bankrupt should not be chosen to act as counsel for the trustee, under the facts of this case we find no such conflict of interest between the Melcher interests and the trustee as to the status of these

Rosenthal interest claims as would require that we reverse the decision of the referee approving this representation.

The Rosenthal interests also attack the referee's action in disallowing their claims for various legal, financial, and management services which, allegedly, they rendered to the bankrupt and for which they were not compensated. In denying these claims the referee found that "the claimants' records were so unreliable and untrustworthy and had been so badly impeached that they could not serve as a basis for allowance for any parts of the claims." There is more than ample evidence in the record to support this finding.

Nor do we find error by the referee in terminating the hearing on the claims presented by Rosenthal and his associates. The referee found that Rosenthal was not acting in good faith during the hearings on the validity of claims, but was intentionally delaying this part of the action. His techniques for obstructing the progress of these proceedings included failure to appear at hearings, frequent and unmeritorious excuses for walking out of depositions, refusals to answer interrogatories, repeated dilatory pre-trial motions and requests for continuances, and obstinate conduct while on the witness stand. While a litigant cannot be denied a hearing merely because he is in contempt, see Hovey v. Elliot, 167 U.S. 409, 17 S. Ct. 841, 42 L.Ed. 215 (1897); Deauville Associates, Inc. v. Eristavi-Tchitcherine, 173 F. 2d 745 (5th Cir. 1949), he is not entitled to continue to obstruct and delay the business of the court after fair and clear warning. Rosenthal was given a full and fair opportunity to be heard; he cannot now complain of the termination of his day in court because of his arbitrary refusal to participate, which had as its only apparent purpose the forestalling of a just determination of the issues on their merits. Rosenthal is therefore deemed to have waived his right to now present

additional evidence. See Lindner v. Kelsheimer, 289 F. 2d 340 (2d Cir. 1961).

The judgment of the court below is in all respects

AFFIRMED.

United States Court of Appeals

FOR THE FIFTH CIRCUIT

October Term, 1972

No. 72-1273

D. C. Docket No. Bk 3-1210

In The Matter of: DALLAS CABANA, INC., Bankrupt.
DALLAS CABANA, INC., ET AL,

Appellants,

versus

WILSON F. COLLIER, Trustee,

Appellee.

Appeal from the United States District Court for the Northern District of Texas

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Before GEWIN, THORNBERRY and CLARK, Circuit Judges.

JUDGMENT

This cause came on to be heard on the transcript of the record from the United States District Court for the Northern District of Texas, and was argued by counsel;

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this Court that the order of the District Court appealed from, in this cause be, and the same is hereby, affirmed;

It is further ordered that appellants pay to appellee the costs on appeal to be taxed by the Clerk of this Court.

November 10, 1972

Issued as Mandate:

In the

United States Court of Appeals

FOR THE FIFTH CIRCUIT

No. 72-1273

In The Matter of: DALLAS CABANA, INC., Bankrupt.
DALLAS CABANA, INC., ET AL,

Appellants,

versus

WILSON F. COLLIER, Trustee,

Appellee.

Appeal from the United States District Court for the Northern District of Texas

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ON PETITION FOR REHEARING AND PETITION FOR REHEARING EN BANC
(Opinion Nov. 10, 1972, 5 Cir., 1972, ____ F. 2d ____).

(December 29, 1972)

Before GEWIN, THORNBERRY and CLARK, Circuit Judges.

PER CURIAM: The Petition for Rehearing is DENIED and no member of this panel nor Judge in regular active service on the Court having requested that the Court be polled on rehearing en banc, (Rule 35 Federal Rules of Appellate Procedure; Local Fifth Circuit Rule 12) the Petition for Rehearing En Banc is DENIED.

In the

United States District Court

FOR THE NORTHERN DISTRICT OF TEXAS

Dallas Division

No. BK-3-1210
(B-3-1213 consolidated for all purposes with BK-3-1210)

In The Matter of: DALLAS CABANA, INC., Debtor.

ORDER

The above-captioned matter came on for hearing before the Court on the third day of November, 1971. The below listed attorneys were present, representing parties stated:

William VanDercreek, Paul H. Stanford, David Musslewhite, and Richard A. Moore, representing Cabana Management, Inc., Rosenthal & Green, and Jerome B. Rosenthal; Jim K. Choate, Stephen Swayze, and James A. Kilgore, representing Dallas Cabana, Inc., in BK-3-1210; William J. Rochelle, Jr. and J. Ronald Trost, representing Dallas Cabana, Inc., in BK-3-1213, and acting as special counsel for the Trustee; Jay Ungerman and Philip I. Palmer, Jr., representing the Trustee; John D. Harris, representing the estate of Martin Melcher; and Marshall Simmons, representing Hyatt Corporation.

The Honorable Elmore Whitehurst, Referee in Bankruptcy, has certified to this Court proceedings in this matter in which the following petitions for review of orders entered by the Referee have been filed:

1) Petition filed in No. BK-3-1210, February 27, 1969, by Dallas Cabana, Inc., by attorney Hubert D. Johnson, for review of order dated February 17, 1969;

2) Petition filed in BK-3-1210, May 12, 1969, by Dallas Cabana, Inc., by attorney Hubert D. Johnson and by Cabana Management, Inc., Jerome B. Rosenthal, and Rosenthal & Green, by attorney James A. Kilgore, for review of order dated May 2, 1969;

3) Petition filed in BK-3-1210, on May 23, 1969, by Jerome B. Rosenthal, Rosenthal & Green, and Cabana Management, Inc., by attorney Hubert D. Johnson, for review of order dated May 19, 1969;

4) Petition filed on May 29, 1969, by Jerome B. Rosenthal, Rosenthal & Green, and Cabana Management, Inc., by attorney James A. Kilgore, for review of order dated May 19, 1969;

5) Petition filed on June 30, 1969, by Jerome B. Rosenthal, Rosenthal & Green, and Cabana Management, Inc., by attorneys Atwell, Malouf & Musslewhite, for review of order dated June 24, 1969;

6) Telegraphic petition filed on July 7, 1969, by Jerome B. Rosenthal, for review of order dated June 27, 1969;

7) Petition filed on July 17, 1969, by Dallas Cabana, Inc., "pro se," by Rose Sammet, as acting secretary, and J. B. Rosenthal, as acting director, for review of order dated July 7, 1969;

8) Petition filed on August 22, 1969, by Rosenthal & Green, Cabana Management, Inc., and Jerome B. Rosenthal, by attorneys Atwell, Malouf & Musslewhite and William VanDercreek, and by Dallas Cabana, Inc., by attorney James K. Choate, for review of order announced August 12, 1969, and entered by the Referee on August 28, 1969;

9) Petition filed on November 24, 1969, by Jerome B.

Rosenthal, Rosenthal & Green, and Cabana Management, Inc., by attorneys William VanDercreek, Paul H. Stanford, and Anthony Atwell, for review of order announced November 14, 1969 and entered by the Referee on December 23, 1969;

10) Petition filed on December 17, 1969, by Jerome B. Rosenthal, Rosenthal & Green, and Cabana Management, Inc., by attorneys William VanDercreek, Paul H. Stanford, and Anthony Atwell, for review of order announced December 8, 1969 and entered by the Referee on December 23, 1969;

11) Petitions filed on December 17, 1969, by Jerome B. Rosenthal, Rosenthal & Green, and Cabana Management, Inc., by attorneys William VanDercreek, Paul H. Stanford, and Anthony Atwell, for review of orders entered December 8, 1969;

12) Petition filed on March 11, 1970 and refiled on March 23, 1970, by Rosenthal & Green and Cabana Management, Inc., by attorneys William VanDercreek, Paul H. Stanford, and Anthony Atwell, for review of order announced March 3, 1970, and entered March 13, 1970.

The Court having duly considered the aforementioned petitions for review, the record of the proceedings before the Referee, the briefs and papers filed herein, and argument of counsel, and being fully advised in the premises, the Court is of the opinion and finds that the aforementioned orders of the Referee, being all of the orders under review, are fully supported by all of the credible evidence and should be affirmed.

Now, therefore, the Court hereby adopts the findings of fact and conclusions of law made by the Referee in Bankruptcy

in these proceedings as set forth in his Certificates of Review filed herein on August 12, 1969, September 8, 1969, February 10, 1970, and May 7, 1970.

It is hereby ORDERED, ADJUDGED and DECREED that all of the aforementioned petitions of Dallas Cabana, Inc., Rosenthal & Green, Cabana Management, Inc., and Jerome B. Rosenthal for review of the aforesaid orders of the Referee in Bankruptcy be and are hereby DENIED; and such orders of the Referee are in all things AFFIRMED;

And it appearing that the taking of further evidence or allowance of further discovery in this matter would unnecessarily delay and impede the disposition of the issues raised by the petitions for review and is not in the interest of the creditors or the debtor and is not in the interest of justice, therefore, all motions, petitions and papers requesting the taking of further evidence and discovery are hereby DENIED.

The Court finds that the Motion to Disqualify J. Ronald Trost and William Rochelle as special counsel to the Trustee and Philip I. Palmer as co-counsel for the Trustee, filed in this Court on February 27, 1970, by Jerome B. Rosenthal, Rosenthal & Green, and Cabana Management, Inc., by attorneys William VanDercreek and Paul H. Stanford, and the Motion for Removal of Trustee and Appointment of Successor Trustee, filed in this Court on September 7, 1971, by Cabana Management, Inc., Rosenthal & Green, and Jerome B. Rosenthal, by attorneys William VanDercreek, Paul H. Stanford, and Richard A. Moore, should be and are hereby DENIED.

SIGNED and ORDERED ENTERED this 3rd day of November, 1971.

/s/ JOE E. ESTES

United States District Judge

APPENDICES

1. 11 U.S.C. § 11(a) (17) (Section 2(a) (17) of the Bankruptcy Act).

(a) The courts of the United States hereinbefore defined as courts of bankruptcy are hereby created courts of bankruptcy and are hereby invested, within their respective territorial limits as now established or as they may be hereafter changed, with such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in proceedings under this title, in vacation, in chambers, and during their respective terms, as they are now or may be hereafter held, to —

(17) Approve the appointment of trustees by creditors or appoint trustees when creditors fail so to do; and, upon complaints of creditors or upon their own motion, remove for cause receivers or trustees upon hearing after notice.

4. 18 U.S.C. § 3057.

(a) Any referee, receiver, or trustee having reasonable grounds for believing that any violations of the bankruptcy laws or other laws of the United States relating to insolvent debtors, receiverships or reorganization plans has been committed, or that an investigation should be had in connection therewith, shall report to the appropriate United States attorney all the facts and circumstances of the case, the names of the witnesses and the offense or offenses believed to have been committed. Where one of such officers has made such report, the others need not do so.

(b) The United States attorney thereupon shall inquire into the facts and report thereon to the referee, and if it appears probable that any such offense has been com-

mitted, shall without delay, present the matter to the grand jury, unless upon inquiry and examination he decides that the ends of public justice do not require investigation or prosecution, in which case he shall report the facts to the Attorney General for his direction.

5. 11 U.S.C. § 72. Trustees; creditors' committees; and attorneys

(a) The creditors of a bankrupt, exclusive of the bankrupt's relatives or, where the bankrupt is a corporation, exclusive of its stockholders or members, its officers, and the members of its board of directors or trustees or of other similar controlling bodies, shall, at the first meeting of creditors after the adjudication, or after a vacancy has occurred in the office of trustee, or after an estate has been reopened, appoint a trustee or three trustees of such estate. If the creditors do not appoint a trustee or if the trustee so appointed fails to qualify as herein provided, the court shall make the appointment. If the bankrupt is a face-amount certificate company, as defined in section 80a-4 of Title 15, the court alone shall make the appointment; but the court shall not make such appointment without first notifying the Securities and Exchange Commission and giving it an opportunity to be heard.

(b) Such creditors may, at their first meeting, also appoint a committee of not less than three creditors, which committee may consult and advise with the trustee in connection with the administration of the estate, make recommendations to the trustee in the performance of his duties and submit to the court any question affecting the administration of the estate.

(c) An attorney shall not be disqualified to act as at-

torney for a receiver or trustee merely by reason of his representation of a general creditor.

6. Bankrutpcy General Order 44.

No attorney for a receiver, trustee or debtor in possession shall be appointed except upon the order of the court, which shall be granted only upon the verified petition of the receiver, trustee or debtor in possession, stating the name of the counsel whom he wishes to employ, the reasons for his selection, the professional services he is to render, the necessity for employing counsel at all, and to the best of the petitioner's knowledge all of the attorney's connections with the bankrupt or debtor, the creditors or any other party in interest, and their respective attorneys. If satisfied that the attorney represents no interest adverse to the reciever, the trustee, or the estate in the matters upon which he is to be engaged, and that his employment would be to the best interests of the estate, the court may authorize his employment, and such employment shall be for specific purposes unless the court is satisfied that the case is one justifying a general retainer. If without disclosure any attorney acting for a receiver or trustee or debtor in possession shall have represented any interest adverse to the receiver, trustee, creditors or stockholders in any matter upon which he is employed for such receiver, trustee, or debtor in possession, the court may deny the allowance of any fee to such attorney, or the reimbursement of his expenses, or both, and may also deny any allowance to the receiver or trustee if it shall appear that he failed to take diligent inquiry into the connections of said attorney.

Nothing herein contained shall prevent the judge, in proceedings under section 77 of the Act, from authorizing

the employment of attorneys who are attorneys of the corporation, or associated with its legal departments, in connection with the operation of the business of the corporation by a trustee or trustees under subsection (c) of section 77, when such employment is found by the judge to be in the public interest in relation to such operation and is not adverse to the interests of the trustee or trustees or of the creditors of the corporation.

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11 USC 69

"Section 69. Contempts before Referees

(a) A person shall not, in proceedings before a Referee (2) misbehave during a hearing • • •

(b) The Referee shall forthwith certify the facts to the judge, if any person shall do any of the things forbidden in this section, and he may serve or cause to be served upon such person an order requiring such person to appear before the judge upon a day certain to show cause why he should not be adjudged in contempt by reason of the facts so certified . . . July 1, 1898, c. 541, Section 41, 30 Stat. 556; June 22, 1938, c. 575, Section 1, 52 Stat. 859.

72-1150

MAR 15 197

MICHAEL RODAK, JR.,

In the

Supreme Court of the United States

OCTOBER TERM, 1972

No. .....

In the Matter of DALLAS CABANA, INC., Bankrupt, JEROME B. ROSENTHAL, ROSENTHAL and GREEN, CABANA MANAGEMENT, INC. and DALLAS CABANA, INC. (BK3-1210),

Petitioners,

v.

WILSON F. COLLIER, Trustee,

Respondent.

Brief in Opposition to Petition For Writ of Certiorari

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REPLY BRIEF NOT PRINTED

TABLE OF CONTENTS

	Page
LIST OF AUTHORITIES	ii
OPINION BELOW	1
RESTATEMENT OF QUESTION PRESENTED	1
STATEMENT OF THE CASE	2
ARGUMENT AND AUTHORITIES	5
1. There is no conflict of interest when the Trustee employs the attorney for the bankrupt as special counsel upon a specific matter involving no conflict in duties	5
2. Petitioners were not denied a hearing on their various motions to disqualify counsel	7
3. There was full compliance with General Order 44	9
4. A Court may rule against a claimant who refuses to submit himself to cross-examination	9
5. No justification exists for issuance of certiorari	11
APPENDIX	A-1

Page

A.B.A. Canon 6 6-7

Bankruptcy General Order 44 ..... 7, 9

Doanbuy Lease Co. v. Melcher, 488 P. 2d 339 (N. Mex. Sup. Ct., 1971) 11

Federal Rules of Civil Procedure, Rule 37(a)(3) 10

Federal Rules of Civil Procedure, Rule 37(b)(2)(B) 11

Illinois v. Allen, (1970) 397 U.S. 337 11

Rosenthal v. Rosenthal, 197 C. App. 2d, 17 Cal. Reptr. 186 (1961) 11

In the

Supreme Court of the United States

OCTOBER TERM, 1972

No. .....

In the Matter of DALLAS CABANA, INC., Bankrupt, JEROME B. ROSENTHAL, ROSENTHAL and GREEN, CABANA MANAGEMENT, INC. and DALLAS CABANA, INC. (BK3-1210),

Petitioners,

v.

WILSON F. COLLIER, Trustee,

Respondent.

Brief in Opposition to Petition For Writ of Certiorari

OPINION BELOW

The opinion below is reported in 469 F. 2d 660.

RESTATEMENT OF QUESTIONS PRESENTED

Neither of the "Questions Presented" as set forth in Petitioner's Brief are raised by the record below. Petitioner's problem is not that he was denied a hearing on disqualification, but that the grounds he alleges for disqualification are being held insufficient as a matter of law. The issue actually raised by the case might be fairly stated as follows:

May a Trustee in Bankruptcy engage as special counsel for

a specific matter or purpose one who is also the attorney for the bankrupt.

By the same token, the Referee in Bankruptcy did not "Summarily punish" Petitioners because he "personally deemed" their actions offensive as Petitioners assert in their second question. The question actually raised by this case is "may a Referee in Bankruptcy sustain a Trustee's objection to a Proof of Claim when the proponent of the claim refuses to submit to cross-examination by the Trustee at the objection hearing."

STATEMENT OF THE CASE

Respondent does not agree with the accuracy of the statement of the case as set forth in Petitioner's Brief. Regrettably, some factual statement is necessary to set the peculiar flavor of this case.

Jerome B. Rosenthal (Rosenthal and Green) served from 1960 to 1968 as the attorney, accountant, business manager, and financial advisor to the Melchers. After the death of Martin Melcher, he also served for a period as counsel for the Melcher probate proceedings.[1] The termination by the Melchers of further representation of them by Rosenthal has lead to an intense, emotional hostility between those parties, which surfaces from time to time in the bankruptcy proceeding. (Tr. 600).

Among the several investments Rosenthal made for the Melchers was the Dallas Cabana, Inc. (the bankrupt). The vehicle for this investment was to have been a limited partnership, although one was never formed. (Tr. 613, 622). Rosenthal

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[1] This was at a time when he also held disputed claims of debt and title in the same estate.

took over actual management of the hotel, which he retained until he turned it over to Wilson F. Collier, Trustee, after this proceeding was filed. (Tr. 3156). Cabana Management, Inc., Rosenthal as president, had been formed as the management entity and was, supposedly, to receive 1% of the gross revenue for its fee. (Tr. 622, 3187).

The operation of the hotel was never profitable, but managed to survive only because Rosenthal continued to advance Melcher funds to cover the losses. (Tr. 621-622, 3182). After the termination of Rosenthal and the employment of new counsel,[2] the Melchers refused to advance any further funds. The predictable result was not long in happening, and reached a crisis when the holder of the first lien announced its intention to foreclose.

To halt this action, Rosenthal filed a petition for an Arrangement Under Chapter XI, obtaining a temporary injunction against the foreclosure. (Tr. 591, 3160). A few days later, a second petition for an Arrangement was filed for the same corporation with the same hotel, but showing a different set of officers and directors. This second proceeding is the one in which J. Ronald Trost[3] and William J. Rochelle, Jr. appear as the attorneys for the Debtor-Bankrupt.

Although Rosenthal apparently conceded the corporate ownership of the hotel when he filed the petition for the Arrangement and obtained the injunction, he seemingly reversed that

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[2] The attorneys for Doris Day Melcher throughout these proceedings have been Chester A. Lappen and John D. Harris, while William A. McKenzie represents the estate of Martin M. Melcher. Neither of the bankrupt's attorneys have ever represented either of the Melchers.

[3] Then with the firm of Quittman, Stuttman, Treister and Glatt, but now with Shutan and Trost.

position, when he discovered that Wilson F. Collier had no intention of returning management to Rosenthal, and further that a prospective cash buyer was then available at a figure sufficient to pay all trade debt and liens. In his new position, Rosenthal contended the bankrupt did not own the hotel, but instead it belonged to a partnership not in bankruptcy.[4] Under the new thesis, the Trustee no longer had any right to the hotel but he and the trade creditors should sue Doris Day Melcher (as a solvent partner) both for her partner's liability and upon breach of her "duty" to continue to cover the losses. This is the title contest which was the major issue upon the merits.

The other issue upon the merits was that of the creditor claims of Petitioners. A Plan of Arrangement was actually filed by Dallas Cabana (the Melcher version) under which the hotel would have been sold to Donald K. Pritzker of the Hyatt Corporation.[5] As with any Plan of Arrangement, it must be approved by a majority of the unsecured claims, both in number and amount, before it can be considered for confirmation. When the Plan of Arrangement was first presented, the claims filed by the Petitioners totalled $558,262.00. The proposed Plan of Arrangement was approved by 100 creditors in an amount of $1,862,000.00. At this point, it appeared Petitioners would be outvoted, however, they then filed amendments to both claims, raising the total to $2,296,176.34. As a result, the Rosenthal

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[4] The only evidence of partnership which petitioners could produce were the tax returns of the Melchers, which they themselves had prepared.

[5] The hotel was ultimately sold by the Trustee to Donald K. Pritzker for $4,350,000.00. The Trustee had first reported a sale to one Howard Johnson for $4,500,000.00 but the latter never made the required cash deposit.

interests claimed over 51% of the total debt and enjoyed a "veto" power over any Plan of Arrangement. (Tr. 3157-8). The amount sought, incidentally, is in addition to the $2,192,724.00 actually paid to Petitioners by the Melcher interests during this same period.

ARGUMENT AND AUTHORITIES

1. THERE IS NO CONFLICT OF INTEREST WHEN THE TRUSTEE EMPLOYS THE ATTORNEY FOR THE BANKRUPT AS SPECIAL COUNSEL UPON A SPECIFIC MATTER INVOLVING NO CONFLICT IN DUTIES.

Of course the attorney for the bankrupt should not be the attorney for the Trustee but that obvious fact does not control this case. The attorneys for the Trustee are Jay W. Ungerman and Philip I. Palmer, Jr. Neither they, nor any member of their firms have ever had any connection of any kind with either Dallas Cabana, Inc. or any of its principals. There has never been any challenge by Respondents to the accuracy of that statement.[6]

At the outset, the Trustee (then Receiver) and his attorneys, Ungerman and Palmer, were presented with two radically different versions of the bankrupt, its assets and liabilities. These attorneys visited with both sides, and their attorneys, investigated the available evidence and reached the firm conclusion that the Melcher version was not only correct in law and fact but was also by far the better course for the unsecured creditors. The

[6] The application to remove counsel filed with the Referee did include Philip I. Palmer, Jr. because he was "actively engaged, along with J. Ronald Trost, in connection with the conduct of this litigation and should be disqualified as co-counsel for the Trustee for the same reasons". The challenge was dropped from the similar motion filed with the District Court and was not raised again on the appeal.

claims could be paid in full by the Melcher version but would receive nothing from the Rosenthal position.

When confronted with these two views, the Trustee was entitled to and did receive independent legal analysis and impartial investigation to reach his decision. Just reaching a decision does not end the Trustee's duty, however, for he is now charged with carrying out that which he has determined to be in the best interests of creditors. Specifically, in this case, he must dispose of the contention that the hotel was not in the bankruptcy court; he must sell the hotel at a price sufficient to pay all legitimate claims, and third; he must see that neither the Melcher nor the Rosenthal claims share equally with trade creditors.

It was concluded that the title question and the challenge to the Rosenthal creditor claims would involve considerable documentary background going back some ten years, much of which was located in California. Rather than charge the time to educate themselves upon these matters, it seemed more economical and swifter to employ the attorneys for the bankrupt to handle both the title contest and the challenge of the Rosenthal claims. Since these attorneys had already prepared themselves to litigate these same issues in the aborted arrangement proceeding there seemed to be no justification in duplicating the time already spent. Although on these issues, both the Trustee and Bankrupt (Melcher version) were in complete agreement, this is the conflict of interest to which so much time has been devoted by Petitioners.

A conflict of interest exists, of course, "when, on behalf of one client, it is his duty to contend for that which duty to another

client requires him to oppose". *A.B.A. Canon* 6. "No interest adverse * * * in the matters upon which he is to be engaged * * *" *Bankruptcy General Order* 44.

Even though Trost and Rochelle never actually represented any of the Melchers, since they were engaged to represent the Melcher version of the bankrupt it can be fairly assumed they are friendly to the Melcher interests. Accordingly, it would have been a conflict of interest to have hired Trost and Rochelle to contest the objection to the Melcher claims[7] but there would seem to be no conflict to engage them on matters upon which the Trustee and the Melcher interests are in complete agreement.

2. PETITIONERS WERE NOT DENIED A HEARING ON THEIR VARIOUS MOTIONS TO DISQUALIFY COUNSEL.

Petitioners were permitted to take depositions of J. Ronald Trost, Chester A. Lappen, Francis Quittner, and Donald K. Pritzker.[8] As a result of this extensive discovery, Petitioners alleged the specific grounds upon which their claim of conflict of interest is based. The Referee and District Judge Estes[9] were simply holding that as a matter of law the recited grounds were not conflicts of interest. Petitioners were permitted oral argument before each forum, the depositions upon which Petitioners rely have been considered and petitioners have at no point suggested any other or further evidence or even a suspicion of

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[7] These objections were filed and handled solely by Palmer and Ungerman for the Trustee, Harris and McKenzie for the claimants.

[8] Petitioners also deposed the attorney for Pritzker, Doris Day Melcher, her son, her accountant and five other principals and attorneys. (Tr. 3166).

[9] Also District Judge Taylor if the independent law suit filed by Petitioners against Referee Whitehurst be considered. (Tr. 3159-60)

further evidence that could be developed by further discovery.

Due process requires that each party litigant be entitled to raise and present his contentions. If those contentions are found wanting in merit, however, the court may rule, even on the pleadings. To illustrate the point by a *reductio ad absurdum*, if Petitioners contended that counsel were disqualified to serve because they were Jewish, due process would require no extended hearing.

The basic "conflict" that Petitioners set forth (Page 9, Petitioner's Brief) is as follows:

> "Rosenthal contended that the Melcher interests wanted to sell the hotel to Pritzker, and discovered that at an undisclosed meeting a deal had been made to sell the assets of the estate and that the bankruptcy forum would be used to give good title".

Instead of creating a conflict, this destroys a conflict for the Trustee also wanted to sell the hotel to Pritzker, made a deal to that effect and is (hopefully) using the bankruptcy forum to give good title. Trost and Rochelle disclosed their "undisclosed meeting" when they filed their Plan of Arrangement in the Chapter XI proceedings. The Trustee disclosed his "undisclosed meeting" when he filed an application to confirm sale to Pritzker. Not only is the agreement destructive of a "conflict" but the Respondent simply cannot conceive of any Trustee who would ever adopt the Rosenthal position and agree to give up the estate and have the creditors receive nothing. The Trustee here would, and should, oppose anyone who tried to take away the hotel. If the Melchers agree with that basic objective they may work together for that specific goal. On the other hand, should

the Melchers have disagreed with the Trustee then they would be opposed along with anyone else who stood in the way of payment to genuine creditors.

3. THERE WAS FULL COMPLIANCE WITH GENERAL ORDER 44.

Petitioners really put their question presented upon the ground that there was inadequate disclosure under General Order 44. Since that order is intended solely to expose possible conflicts of interest, Respondent has treated the conflict question as the basic issue. The text of the original affidavit is attached as an appendix to this brief, and discloses all connections by the special counsel to the bankrupt, possible principals and the source and amount of their fees.

The "undisclosed meeting" with Pritzker is the only fact which Petitioners assert should have been disclosed. (P. 5, Petitioners' Brief) Not only had it already been fully disclosed[10] but it posed no possible conflict since the Trustee was not bound by any agreement for sale the bankrupt might have had.[11]

4. A COURT MAY RULE AGAINST A CLAIMANT WHO REFUSES TO SUBMIT HIMSELF TO CROSS-EXAMINATION.

Petitioners would give the impression that they were given no opportunity to present their evidence when in fact the hearing went nine trial days and had over three hundred exhibits introduced.

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[10]Rochelle and Trost had already filed the unsuccessful Plan of Arrangement trying to sell the hotel to Pritzker.

[11]which is why the Trustee could try to sell to Howard Johnson for a higher price.

The Referee covers, in his certificate of review of May 7, 1970, (Tr. 3152-3210) the conduct of Petitioners in great detail. Before trial even commenced, Petitioners filed five motions for continuance and six other dilatory motions. There were also three refusals of Rosenthal to appear or testify during the trial, two refusals to appear for depositions, one refusal to obey an order to produce documents, and one refusal to answer written interrogatories.

Now Petitioner contends that he was punished for contempt, but that simply was not what happened. Rosenthal had testified on direct examination by his own attorneys but refused to take the stand to undergo cross-examination by the attorneys for the Trustee. (Tr. 3174). The Referee granted a short recess but gave warning that unless Rosenthal retook the witness stand he would deny the claims by default. (Tr. 3175).

Rosenthal did in fact take the stand, but by a variety of thinly veiled pretenses refused to answer any questions.[12] As a trained lawyer with over thirty years of experience, Rosenthal is exceedingly skilled in those tactics which bring about the result he desires. An evasive or incomplete answer is the same as a failure to answer, *Rule 37(a)(3) Federal Rules of Civil Procedure.* By the same rule, failure to answer questions after being directed

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[12]He couldn't say when he first rendered services to the hotel because "hotels can't have services rendered to them, they are collections of objects". (Tr. 3178). He couldn't say whether his law firm kept separate records of services to the bankrupt because "again, I must remind you that law firms by that designation are collective and do not refer to the individuals within it that comprise the law firm". (Tr. 3179) The efforts of the Trustee to cross-examine Rosenthal continued for a considerable period. The foregoing are only typical examples of the frustration tactics of Petitioners.

so to do is grounds for judgment by default. *Rule 37(b)(2)(B) Federal Rules of Civil Procedure.* While good grounds doubtless also existed for which the Referee could have certified Rosenthal to the District Court for contempt, that was not done.

This particular tactic has occurred before other courts by the same Rosenthal to the point that it becomes a pattern of conduct bearing upon evidence of good faith. Speaking of Rosenthal, the California Court of Appeals remarked about:

> "* * * persistently technical and dilatory opposition * * *"
>
> * * * * *
>
> "* * * recurring offensive conduct and language toward the judge." *Rosenthal v. Rosenthal,* 197 C. App. 2d 289, 17 Cal. Rptr. 186 (1961)

Even more precisely in point is the observation of the Supreme Court of New Mexico,

> "The statements of Mr. Rosenthal consisted of evasions, expressions of hostility, insults, admonitions, objections, demands that counsel explain what bearing questions had upon the issues as pre-requisite to answers, arguments and other similar responses." *Doanbuy Lease Co. v. Melcher,* 488 P. 2d 339 (N.M. Sup. Ct. 1971).

As this court has observed, in the more difficult area of criminal justice, the trial court has wide discretion in presenting flagrant disregard of elementary standards of proper conduct. *Illinois v. Allen,* (1970) 397 U.S. 337, 343.

5. NO JUSTIFICATION EXISTS FOR ISSUANCE OF CERTIORARI.

Petitioner brings forth no questions dealing with the merits. Instead he seeks to pose over-broad questions said to involve

important issues of Federal law. In truth, however, the genuine issues are narrow factual points, of importance only to this specific case. These factual issues have already been presented to three courts, and all have decided, without dissent, against the contentions of Petitioner. Litigation must end at some point with the reluctant losers held to have had not only their day in court but also their appeal.

CONCLUSION

The Petitioner for Writ of Certiorari should be denied.

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APPENDIX TO BRIEF

STATE OF TEXAS }
COUNTY OF DALLAS }

BEFORE ME, the undersigned authority, on this day personally appeared Philip I. Palmer, Jr. and William J. Rochelle, Jr., each of whom being first duly sworn by me, deposed and said that they are representatives of the firms constituting proposed general counsel for the Trustee and Special Counsel for the Trustee, respectively, and that neither they nor any member of the firms named represent any interest adverse to the Trustee upon the matters for which they are to be employed to the best of their knowledge, information and belief. Proposed special counsel would disclose in this regard that they received $10,000 in retainer checks plus $1500 for expenses after filing of the Chapter XI Petition herein which checks were drawn on the bank account of Doris Day Melcher and that although they understand that said checks constituted an advance by Doris Day Melcher on behalf of the bankrupt corporation, they do not know this of their personal knowledge. However, Affiants do not now nor have they ever represented Doris Day Melcher or the Estate of Martin Melcher, Deceased. Further, Quittner, Stuttman, Triester & Glatt have been employed by Palo Alto Inn, Inc., which is principally owned by Doris Day Melcher and Terrence Paul Melcher, in connection with its financial problems. Also, Quittner, Stuttman, Triester and Glatt represented C. S. Heinz and C. S. Heinz Enterprises in connection with a Chapter XI proceeding in California which was confirmed in 1967.

/s/ PHILIP I. PALMER, JR.

Philip I. Palmer, Jr.

/s/ WILLIAM J. ROCHELLE, JR.

William J. Rochelle, Jr.

SUBSCRIBED AND SWORN TO BEFORE ME, this the 9th day of May, 1969.

/s/ BARBARA ANN COLLINS

Notary Public in and for
Dallas County, Texas